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UNCLAS SECTION 01 OF 03 KUALA LUMPUR 001942

SIPDIS

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STATE PASS USTR - WEISEL, JENSEN AND MAIN
STATE PASS FEDERAL RESERVE SAN FRANCISCO TCURRAN
STATE PASS EXIMBANK
USDOC FOR 4430/MAC/EAP/J.BAKER
TREASURY FOR OASIA AND IRS
GENEVA FOR USTR

E.O. 12958: N/A
TAGS: [ECON](#) [EFIN](#) [ETRD](#) [EXIM](#) [PHUM](#) [PREL](#) [MY](#)
SUBJECT: FOLLOW THE MONEY: THE POLITICS OF SHARE OWNERSHIP
IN MALAYSIA

REF: KUALA LUMPUR 0930

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¶1. (SBU) Summary: A report by a respected local think tank has sparked a political uproar by claiming that ethnic Malays already control more than the government's target of 30% of the shares on the KL Stock Exchange (KLSE). As the 30% goal provides the underlying rationale for the bumiputera policy, the pervasive system of socioeconomic preferences for Malays and other indigenous peoples, the idea that this target might have been achieved is political dynamite. The government's own statistics indicate that bumiputeras own only 18.9% of the KLSE. Deputy PM Najib quickly defended this figure and said that further dispute "could hurt the feelings of certain races and could be regarded as sedition even though that was not the intention." The president of the think tank retracted the report, but the chief author stood by his work and resigned in protest. The argument over the numbers brings to mind Mark Twain's admonition about "lies, damn lies and statistics," but the uproar it sparked highlights the continuing tensions between the different ethnic communities in Malaysia. Anything touching on the fundamental bargain between the politically dominant Malays, and the economically connected Chinese, remains extremely sensitive in this country. End summary.

Background: The Bumiputera Policy

¶2. (U) In response to race riots in 1969, the government of Malaysia launched the "New Economic Policy" (NEP), which aimed to strengthen national unity, eradicate poverty and address the economic imbalances between the races in Malaysia (reftel). At that time, the government estimated that bumiputeras (ethnic Malays and a small population of indigenous peoples) owned about 2% of the nation's wealth, non-bumiputeras (mainly Chinese) owned 37% and foreigners owned 61%. The NEP ushered in numerous affirmative action initiatives with the aim of adjusting these shares to 30% bumiputera, 40% non-bumi Malaysians, and 30% foreign owned. The benchmark for measuring wealth was the share of corporate equity on the Kuala Lumpur Stock Exchange (KLSE). The scope of the preferences and privileges granted to bumiputeras has grown through the years, but the ownership

targets have remained out of reach, at least according to government statistics.

Be Careful What You Ask For

13. (U) In the course of preparing the Ninth Malaysia Plan, the Government's five-year economic development framework, Prime Minister Abdullah Ahmad Badawi invited public participation and input, in keeping with promises he made to solicit and accept feedback on social and economic issues. In February 2006, the Center for Public Policy Studies (CPPS), the research arm of the Asian Strategy and Leadership Institute (ASLI), submitted to various government agencies and members of Parliament its analyses and recommendations for the five-year plan. ASLI is a respected local think tank closely associated with the government. The chief author of the report was a former World Bank and UN economist, and the current Director of CPPS Dr. Lim Teck Ghee. Among its numerous conclusions and recommendations, the report questioned the methodology of the Government's calculation of bumiputera corporate equity and suggested that the real figure could be as high as 45 per cent of market capitalization.

A Delayed but Explosive Reaction

14. (U) The CPPS report languished in obscurity and probably had been forgotten by the government officials who had received it. But in September Malaysiakini.com, a local Internet-based news organization, discovered it on CPPS's website, interviewed Lim, and posted a brief article focusing on his estimate of bumi share ownership. Public outcry and government outrage soon followed. Deputy Prime Minister Najib quickly defended the government's figure and said that further dispute "could hurt the feelings of certain races and

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could be regarded as sedition even though that was not the intention." Other political heavyweights piled on, and on October 10 ASLI President Mirzan Mahathir, son of former Prime Minister Mahathir Mohammed, retracted the report. In a statement published on Malaysiakini.com he apologized for "the hurt and confusion felt by all Malaysians caused by the center's report," claimed that there were "shortcomings in assumption and calculation that led to conclusions that could not be vigorously justified," and stated that ASLI felt that the report "did not fairly reflect the true picture of total equity ownership" by Bumiputeras. Lim, however, stood by his team's analysis and announced that he would resign at the end of the month in protest.

Using The Wrong Measuring Stick

15. (U) CPPS's report "Corporate Equity Distribution: Past Trends and Future Policy" identifies several questionable aspects of the government's methodology. First, it points out that corporate equity is only one measure of economic ownership, and trends indicate that bumiputeras often cash out their gains from stock shares. One affirmative action policy reserves 30 per cent of Initial Public Offerings for bumis, typically at a below-market price. The report claims that while a newly-listed corporation may achieve 30% bumiputera ownership at the outset, this figure drops quickly as bumis cash out quickly to lock in profits at market prices. They may not plow these earnings back into the stock market but direct them to other investments, for example into real estate where bumis also can benefit from preferential deals. This drop in corporate equity, CPPS argues, should not be seen as a drop in the proportion of national wealth held by Bumiputeras.

16. (U) The report also pointed out that, while the original goal of the NEP was to attain national unity by eradicating

poverty and addressing economic imbalances, the government's affirmative action policies do not address the distribution of wealth among bumiputeras. It notes that "...if just one Bumiputera came to own most of this corporate equity with all the rest holding little or nothing, the 30 per cent target would still have been achieved."

Slicing the Government's Pie

¶17. (U) Even looking solely at corporate equity, CPPS had concerns about the methodology used in determining the government's figures. Most significantly, it points out that the government owns approximately 36% of the nation's corporate equity, but attributes all of these holdings to the non-bumiputera side of the ledger. The CPPS report maintains that the government should either subtract its holdings from the total and calculate the ethnic shares of the 64% of the of the market available for private ownership, or should proportionately allocate the government's holdings to bumiputera and non-bumiputera in some reasonable fashion. The CPPS study proposed that 70% of government holdings should be counted on the bumiputera side of the ledger, while suggesting that even this allocation was probably too low. Based on this 70% estimate, CPPS calculated that the bumiputera equity share could be as high as 45 per cent.

Lies, Damn Lies, and Statistics

¶18. (U) The government's response to the report asserted that it has better data that includes information on non-publicly traded companies. Government calculations are therefore based on data from 6,000 companies, both public and private, while CPPS's figures are based only on Malaysia's 1011 publicly-traded companies. The government has not, however, responded to CPPS's point about the allocation of government-owned shares to the non-bumi side of the ledger. Using the government's own figures for bumiputera equity, and removing the government owned-shares from the equation yields an estimate that bumis hold 29.53% of the equity that is available for private ownership - statistically indistinguishable from the target of 30%.

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The Third Rail of Malaysian Politics

¶19. Comment: (SBU) The uproar sparked by the CPPS report highlights the continuing tensions between the different ethnic communities in Malaysia. Anything touching on the fundamental bargain between the politically dominant Malays and the economically connected Chinese remains extremely sensitive in this country. The government may be able to control the public debate, but the disconnect between its avowed aims and economic reality will remain a sore point for many.
SHEAR